

Message Text

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SUBJECT: SOVIET UNION AGREES TO EXPORT CRUDE OIL TO INDIA

REF: NEW DELHI A-167 OF JUNE 5, 1976

1. ACCORDING TO FROMT-PAGE ARTICLES IN ALL OF TODAY'S NATIONAL NEWSPAPERS, SOVIET DEPUTY FOREIGN TRADE MINISTER I.T. GRISHIN OFFICIALLY INFORMED GOI DECEMBER 20 THAT THE SOVIET UNION WOULD CONSIDER SUPPLYING ONE MILLION TONS OF CRUDE OIL TO INDIA IN 1977, AND ONE AND A HALF MILLION TONS IN EACH OF THE FOLLOWING THREE YEARS. IN EXCHANGE, INDIANS ANNOUNCED THEY WOULD SELL PIG IRON, STEEL AND OTHER GOODS OF EQUIVALENT WORTH. GOI SPECIFICALLY WAS PREPARED TO SELL 400,000 TONS OF PIG IRON IN 1977. ANNOUNCED VALUE OF SOVIET OIL OFFER FOR 1977 IS RUPEES 800 MILLION (\$91 MILLION AT RS. 8.80 EQUALS \$1). GRISHINS' OFFER CAME ON THE FIRST DAY OF THE TRADE NEGOTTIATIONS AIMED AT PRODUCING FINAL TRADE PLAN FOR 1977 INDO-SOVIET TRADE.

2. BILATERAL TALKS AT EXPERT LEVEL ARE CONTINUING WITH REGARD TO SPECIFICATONS, DELIVERY SCHEDULES AND OTHER DETAILS OF
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SOVIET OIL AND CONTERBALANCING INDIAN ITEMS. THE 1977 TRADE PLAN IS EXPECTED TO BE SIGNED BY THE END OF THE WEEK.

3. PETROLEUM MINISTER MALAVIYA TOLD AN ENERGY-RELATED SEMINAR DECEMBER22, "WE ARE VERY HAPPY AND THANKFUL THAT AT A CRITICAL TIME WE HAVE THE RESPONSE FROM A FRIENDLY COUNTRY FOR MORE

CRUDE OIL." IN THIS CONTEXT HE REITERATED COMPLAINT THAT OPEC COUNTRIES HAD "OBSTNATELY" AND IN "ANGRY MOOD" EFFECTED AN "IRRATIONAL INCREASE" IN OIL PRICES.

4. COMMENT: THE SOVIET OFFER IS A MAJOR BREAKTHROUGH IN INDO-SOVIET ECONOMIC RELATIONS, REPRESENTING AN IMPORTANT ECONOMIC GAIN FOR THE GOI AND POLITICAL CONCESSION BY THE USSR AT--WE BELIEVE-- SOME ECONOMIC COST TO THE RUSSIANS.

5. AS ANALYZED IN REFARIGRAM, INABILITY OF SOVIET UNION TO PROVIDE GROWING VOLUME OF GOODS NEEDED BY INDIAN ECONOMY HAS BEEN SERIOUS CONSTRAINT ON THEIR BILATERAL ECONOMIC TIES. IN PARTICULAR, THE INDIANS HAVE SOUGHT SOVIET CRUDE OIL SINCE 1974, BUT THEY HAD MET WITH SUCH FIRM REBUFF THAT OFFICIALS HAD GIVEN UP HOPE IN EARLY 1976. FROM OUR VANTAGE POINT, SOVIET OFFER--OF WHICH THERE HAD NOT BEEN THE SLIGHTEST HINT BEFORE DECEMBER 20 ANNOUNCEMENT--IS POLITICAL DECISION BY THE SOVIETS TO RESPOND TO INDIAN INTERESTS.

6. BENEFITS TO INDIA ARE TWOFOLD: A REAL FOREIGN EXCHANGE SAVING (AT LEAST IN 1977, AND PERHAPS IN LATER YEARS) AND A SLIGHT REDUCTION IN DEPENDENCE ON MIDDLE EAST OIL SOURCES. FOREIGN EXCHANGE SAVINGS DEPENDS ON TWO FACTORS:

(A) SUBSTITUTION OF SOVIET FOR OPEC OIL: UNTIL YESTERDAY'S ANNOUNCEMENT, GOI POLICY WAS TO KEEP OIL IMPORTS AT CURRENT CEILING (ROUGHLY 14 MILLION TONS) AND MEET EXPANDIGN DEMAND THROUGH DOMESTIC PRODUCTION. THEY NOW HAVE THE OPTION OF EITHER RELAXING IMPORTS SLIGHTLY WITHOUT ADDITIONAL HARD CURRENCY COST, OR CUTTING BACK ON MIDDLE EAST PURCHASES.
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(B) DIVERSION OF INDIAN EXPORT ITEMS FROM HARD CURRENCY MARKETS: PRESS ACCOUNTS OF THE ANNOUNCEMENT ASSERT THAT INDIAN PRODUCTION OF PIG IRON AND STEEL ARE CURRENTLY IN EXCESS OF DEMAND FROM THE DOMESTIC MARKET AND FROM HARD CURRENCY TRADING PARTNERS. OUR QUICK ANALYSIS OF PIG IRON PRODUCTION SUPPORTS THIS CLAIM. TOTAL PRODUCTION FOR THE FIRST SIX MONTHS OF 1976 AT 4.5 MILLION TONS, WAS 500,000 TONS GREATER THAN THE SAME PERIOD IN 1975. YET EXPORTS IN INDIAN FISCAL YEAR 1975-76 (ENDING MARCH 31) TOTALED ONLY 235,000 TONS. OVER LONGER RUN, COMMITMENTS TO SOVIET UNION MIGHT CUT INTO POTENTIAL HARD CURRENCY SALES.

7. WHILE IN SHORT RUN INDIA WILL BE UNDER SOME PRESSURE TO MAINTAIN MIDDLE EAST OIL IMPORTS (E.G., CREDIT SALES, REFINERY PRODUCTION PROGRAMS), IN THE MEDIUM TERM SOVIET IMPORTS WILL REDUCE SOMEWHAT INDIAN DEPENDENCE ON MIDDLE EAST SUPPLIERS. INDIAN DOMESTIC PRODUCTION, WE ESTIMATE, WILL RISE SUFFICIENTLY BY 1978 TO BRING ABOUT A REDUCTION IN TOTAL OIL IMPORTS--ASSUMING

THE CONTINUATION OF CURRENT STRONG RESTRAINTS ON DOMESTIC OIL CONSUMPTION. SOVIET SUPPLIES WILL MAGNIFY THE IMPACT OF THIS TREND ON TRADITIONAL SUPPLIERS.

8. WHILE FOREIGN EXCHANGE AND OIL DEPENDENCY FIGURES CAN BE DETERMINED, REAL ECONOMIC "COST" TO INDIA IS NOT SO EASY TO ESTABLISH. IT IS NOT CLEAR FROM PRESS ACCOUNTS THAT SOVIETS ARE COMMITTED TO RUPEES 800 MILLION FIGURE FOR ONE MILLION TONS OF OIL; IT SEEMS MORE LIKELY THAT FIGURE IS ILLUSTRATIVE, BASED ON CURRENT INDIAN COSTS. CURRENT PRACTICE IN INDO-SOVIET TRADE IS THAT RUPEE PRICE OF GOODS IS DETERMINED BY AGREEMENT BETWEEN BUYING AND SELLING AGENCIES AT TIME CONTRACT SIGNED. QUESTION REMAINS WHETHER SOVIETS WILL SELL AT OPEC PRICE AFTER JANUARY 1 AND NEXT JULY 1-- AND IF SO, WHICH OPEC PRICE?

9. IT IS ALSO UNCERTAIN WHETHER SOVIETS WILL INSIST ON BARGAIN PRICES FOR THE PIG IRON AND OTHER GOODS IT WILL RECEIVE. ACCORDING TO GOI TRADE FIGURES, THE UNIT VALUE OF PIG IRON EXPORTS TO THE LIMITED OFFICIAL USE

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SOVIET UNION WAS SIGNIFICANTLY LOWER (46 PERCENT) THAN THE PRICE TO OTHER FOREIGN CUSTOMERS IN IFY 1974-75 AND SOMEWHAT LOWER (13 PERCENT) THE PRECEDING YEAR. (WE SHOULD NOTE, HOWEVER, THAT STUDIES OF INDO-SOVIET TRADE OF WHICH WE ARE AWARE CONCLUDE THAT OVER TIME AND OVER THE RANGE OF PRODUCTS TRADED, PRICES OF GOODS IN TRADE TEND TO EQUATE TO WORLD PRICES.)

10. GOI OFFICIALS HANDLING SOVIET UNION AND EASTERN EUROPE ARE NOW CAUGHT UP IN ANNUAL RUSH OF VISITING DELEGATIONS. WE SHOULD BE ABLE TO GET THEIR VIEWS DIRECTLY WITHIN A FEW WEEKS AND WILL BE REPORTING FURTHER.
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